

**LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS**

301 State House
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FISCAL IMPACT STATEMENT

LS 6456

BILL NUMBER: HB 1593

DATE PREPARED: Feb 14, 2001

BILL AMENDED:

SUBJECT: Earned Income Tax Credit.

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FUNDS AFFECTED: X

**GENERAL
DEDICATED
FEDERAL**

IMPACT: State

Summary of Legislation: This bill exempts an employer from the state income tax withholding requirements for an employee if the employee certifies to the employer that the employee's wages from the employer will comprise more than 80% of the employee's wages for the calendar year and will not exceed \$15,000.

The bill also increases the qualifying income amount from \$12,000 to \$18,000 under the Earned Income Tax Credit and makes the credit permanent. (Under current law, the credit expires December 31, 2001.)

Effective Date: July 1, 2001; January 1, 2002.

Explanation of State Expenditures: The Department of State Revenue (DOR) will incur some administrative expenses related to the revision of tax forms, instructions, and computer programs to incorporate these changes to the Earned Income Tax Credit and withholding requirements. These expenses could be absorbed given the DOR's existing budget and resources.

Secondary impact: The refundable portion of the Earned Income Tax Credit would qualify as Maintenance of Effort (MOE) expenditures and would contribute toward the state's annual MOE requirement under the Temporary Assistance to Needy Families (TANF) program. *The refundable portion of the earned income credit at the \$18,000 level is estimated to range from \$29.5 M to \$31.5 M .*

Explanation of State Revenues: *The revenue loss from raising the Earned Income Credit to \$18,000 and making the credit permanent is estimated to range from \$42.5 M to \$45.3 M. (of which \$29.5 M to \$31.5 M is estimated to be refundable).* Under current law, the Earned Income Tax Credit is available to individuals who have the following: (1) at least one qualifying child; (2) income from all sources of not more than \$12,000; and (3) at least 80% of total income from earned income. The amount of this refundable credit is equal to \$12,000 minus the taxpayer's total Indiana income. Under this proposal, the \$12,000 upper limit would be increased to \$18,000, thereby expanding the pool of Indiana residents eligible for this tax credit.

1998 individual income tax data from the DOR were used to estimate the fiscal impact of this proposal. The Earned Income Tax Credit did not yet exist, but a similar Earned Income Deduction was available and was claimed on almost 54,000 state tax returns. The impact of converting the deduction to a credit was calculated first. Next, the impact of increasing the income limit to \$18,000 was determined. Summary statistics indicate that increasing the limit from \$12,000 to \$18,000 would have increased the number of eligible taxpayers by almost 76%.

As the credit is set to expire under current law on December 31, 2001, the impact of the proposal is not only the difference between the \$12,000 and \$18,000 scenarios, but rather the full impact of offering the Earned Income Tax Credit with the \$18,000 limit. However, baseline estimates for this analysis were developed using 1998 tax year data. As this credit was relatively new, the revenue loss may be greater in subsequent years as some eligible taxpayers may not have claimed the deduction in 1998.

The DOR reported that for the 1999 tax year, approximately \$16 M in Earned Income Credits were claimed, with \$12.7 M being refundable.

The annual impact would begin in FY 2003 as this proposal is effective January 1, 2002. Individual Adjusted Gross Income Tax revenue is deposited in the General Fund.

Explanation of Local Expenditures:

Explanation of Local Revenues:

State Agencies Affected: Department of State Revenue.

Local Agencies Affected:

Information Sources: Rob Whaley, Tax Policy Analyst, Department of State Revenue, (317) 232-2104; DOR's 1998 individual income tax data.